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High Technology Tort Litigation

Ronald Hayes Malone

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**THE FUTURE OF TORT LITIGATION IN
CALIFORNIA
SANTA CLARA, CALIFORNIA, MARCH 11, 1989**

III. HIGH TECHNOLOGY TORT LITIGATION

A. *Essay—A Proposed Cure for High Technology Tort Abuse*

Ronald Hayes Malone*

1. INTRODUCTION

California tort law is too often used as a tool of oppression rather than as an instrument of justice. This unfortunate phenomenon occurs in many areas, but its manifestations are particularly acute in the high technology area. There the inherent complexity of the underlying technology and the amorphous nature of the legal issues combine with a widespread fear of unpredictable juries and runaway damage awards to make the litigation process obscenely expensive. California tort law—with its exotic new causes of action and incalculable damages—has become an awesome weapon, whether wielded by the big company concerned about losing business to a spin-off or in the hands of a David against a Goliath.

Ever-expanding and omni-present tort concepts, including statutory causes of action such as misappropriation of trade secrets and unfair competition, are the subject of widespread misuse. Unmeritorious tort claims are often injected into ordinary commercial contract disputes because they carry with them “the allure of punitive damages—a golden carrot that entices into court parties who might otherwise be inclined to resolve their differences.”¹ Claims such as promissory fraud, breach of fiduciary duty, tortious breach of the

• 1989 by Ronald Hayes Malone

* Partner, Orrick, Herrington & Sutcliffe, San Francisco, CA; J.D., 1971, Santa Clara University School of Law; L.L.M., 1975, Harvard University; former co-chairman of the 75 lawyer litigation department at Orrick, Herrington & Sutcliffe; the author has a broad range of corporate and commercial litigation experience, representing both plaintiffs and defendants in major cases in state and federal courts.

1. *Oki Am. v. Microtech Int'l*, 872 F.2d 312, 315 (9th Cir. 1989) (Kozinski, J., concurring).

implied covenant of good faith and fair dealing, bad faith denial of contracts, and interference with contractual relations or prospective economic advantage—with their concomitant claims for punitive damages—frequently find their way into such contract disputes with woefully little or no factual justification. Often, the purpose for adding these tort claims is to impose economic leverage where the underlying contractual relationship between the parties provides none and as a means of increasing damage exposure. In short, these pendant tort claims are often used as a means of extorting settlements. Indeed, Judge Kozinski of the Ninth Circuit Court of Appeals recently observed that “[t]his tortification of contract law—the tendency of contract disputes to metastasize into torts—gives rise to a new form of entrepreneurship: investment in tort causes of action. ‘If Pennzoil won \$1 billion from Texaco, why not me?’”²

Once informed of the “rules of the game,” what prudent Silicon Valley executive—no matter what the merits of the case—would willingly bear the enormous burden of attorneys’ fees, expert witness fees, court costs, lost management time and face the incredible uncertainty of a jury trial? Why not just settle? While the early settlement of legitimate disputes should be encouraged, the settlement of cases irrespective of their merits and out of fear of the unpredictability of juries or the high cost of battle is more like making an extortion payment than making a business decision. Such coerced decision-making promotes disrespect for the law, its procedures and its representatives, and eventually breeds lawlessness.

Let’s look at three typical situations that arise in the high technology context.

a. *Start-ups and Spin-offs*

Silicon Valley is the home of more start-up, spin-off and emerging companies than any other place on the planet. Talented and creative engineers move from company to company looking for the right opportunity and environment in which to apply their creative genius. Many believe that the cross-fertilization of ideas associated with this kind of mobility is one of the great engines of technological innovation. Very few founders begin their careers in the company they start-up. Rather, the norm is for them to move from one company to another and then, when they become frustrated or feel stifled as an employee of a larger corporate organization, to strike out on their

2. *Id.* at 315.

own to start a new venture.

Sometimes when they leave, they develop their new venture on the basis of a corporate opportunity misappropriated from their former employer or on stolen trade secrets. When they do, they are justifiably subjected to vigorous prosecution by their former employer. Frequently, however, it is not so simple. When they leave to start up a venture that might compete, directly or indirectly, with their former corporate employer, they are hit immediately with a preemptive trade secret lawsuit. This is the norm, not an aberration. The prevailing big firm, corporate mentality in this context seems to be: "Sue first, and ask questions later." Frequently, when the previous employer files its complaint accusing the former employee of misappropriating trade secrets, it literally has no idea what, if any, trade secrets were actually misappropriated. Instead, it feels justified in filing the complaint on the basis of two facts: the former employee's access to trade secrets, and a potential opportunity to use those trade secrets at the competing company. Having thus rationalized the propriety of filing the lawsuit, the plaintiff proceeds to reap the real benefits from its action: (1) interference with the financing of the spin-off; (2) disruption and distraction of the management of its new competitor; (3) delay of the nascent competitor's new product releases; and (4) reassurance and intimidation of plaintiff's loyal, non-departing employees.

The blameless defendant can choose to fight the lawsuit brought by his Goliath former employer. Assuming that he has the time, inclination, and vast amounts of extra, unneeded capital, he can even declare nuclear war and vigorously pursue a cross-complaint for unfair competition or antitrust violations. But we all know that is not what happens in the real world. Instead, the defendant agrees to a settlement, the typical terms of which include a nominal (and secret) payment, an agreement to be subjected to unannounced technological audits by third-party consultants, and an agreement not to hire any more of plaintiff's employees. His new company may be somewhat hobbled by these terms, but at least it has a chance to survive, which would be much less likely if it had to endure a long, costly court battle.

b. *Lawsuit by Founder After Loss of Control*

Another scenario that has played itself out time and time again in Silicon Valley revolves around the changing role of the founder as his company matures and becomes profitable and the conflicts which develop between that founder and his financial partners. A typical

situation involves the founding of a start-up by a person with market vision or technological innovations, or both. As "his" company grows and he envisions "himself" "going public," he obtains the financing he needs for necessary growth from venture capitalists. As the company grows further and its annual sales reach 25 or 50 million dollars, the founder's financial partners envision someone other than the founder as the firm's CEO as it matures into a soon-to-go-public company. As the founder is eased aside or upstairs—ceremoniously or otherwise—to make room for stronger management, he feels a loss of control, begins to feel as if the company is no longer his, and his alienation and disenchantment grow. When the company performs poorly without the founder at the helm, the fur flies and a lawsuit frequently follows.

Does the founder simply sue for breach of his written employment contract? Of course not; there will be the obligatory causes of action for breach of oral and implied contracts. But he will not stop even there. The plaintiff will add tort claims for breach of the implied covenant of good faith and fair dealing and for interference with prospective economic advantage.

Does he sue only the company? No, he sues the directors and a few officers for the sake of symmetry, knowing full-well that his leverage is increased as a result of a lack of adequate director and officer liability coverage. Typical allegations—all with the benefit of hindsight—might include:

1. Promissory fraud by the venture capitalist for not disclosing its secret intent, harbored at the time of the original investment, to sack the founder and replace him with a Harvard MBA who will subsequently ruin the company.
2. Conspiracy by all of the directors and some of the shareholders to breach various and sundry fiduciary duties.
3. And just to insure the unavailability of the business judgment defense, he will throw in an allegation that his former colleagues, a.k.a. "conspirators," all had improper, corrupt and venal purposes in acting (or voting) as they did.

c. *Commercial Disputes Between Software Companies*

Disputes between software companies are legion in Silicon Valley. Market pressures and technological barriers make disappointment almost inevitable. When an important product is not developed or marketed in accordance with the perceived terms of the written contract and a substantial economic loss falls on one of the parties,

you have the makings of a lawsuit. If the dispute is not resolved amicably, a breach of contract lawsuit will result, correct? Wrong. The plaintiff cannot obtain a windfall, nor any punitive damages, under a straight breach of contract cause of action. Instead, the pleadings will allege not only breach of contract, but also any one or more of the following causes of action:

1. Breach of the implied covenant of good faith and fair dealing.
2. Breach of fiduciary duty (typical allegations include superior knowledge by the defendant and trust and reliance on the part of the plaintiff).
3. Interference with prospective economic advantage (e.g., deprivation of the enormous economic success the company would have enjoyed, but for the treachery of the defendant).
4. Intentional and negligent infliction of emotional distress.
5. Bad faith denial of contract.
6. Perhaps a claim of promissory fraud just to spice things up.

2. ARGUMENT

All of this is done with a cold cynicism on the part of the lawyers. The name of the game is to plead enough to prevent the trial judge from sustaining a demurrer without leave to amend, or granting a motion to dismiss with prejudice. Plaintiffs know that Rule 11 and California Code of Civil Procedure section 128.5 constitute no real threat to them if they are at all artful. They know that claims of abuse of process and malicious prosecution are far-off, difficult for claimants to establish and can be dealt with at the settlement stage. Discovery is conducted with a keen awareness that summary judgment against them on the tort claims—that's where the plaintiff's³ leverage is—can be avoided by creating some triable issue of material fact, no matter how fanciful, small or insignificant.

Thus, plaintiffs frequently append weak (but artfully-pleaded) tort claims to their contract claims with a hope that they might find some factual support for them in discovery (perhaps a carelessly-worded answer to a deposition question) and either roll the dice before the jury or, preferably, settle the case for more than the value of the contract claims. One of the real tragedies of our current sys-

3. The abuse to which this author alludes is not limited to plaintiffs. Cross-complaints by defendants frequently suffer the same shortcomings. As used herein, the term "plaintiff" will include all claimants, whether plaintiffs or cross-complainants.

tem is that plaintiffs are often successful in retaining these weak tort claims through the discovery stage. And because the cases are so complex and defense counsel so afraid of the punitive damage exposure which accompanies the tort claims, by the time the parties arrive at serious settlement discussions, both sides have invested more in attorneys' fees and expert witness fees than the contract claims are worth.

When the process breaks down this way, the result is unhappy clients and wealthy lawyers. Clients too often come away with the perception that success turns not on whether the facts or the law are in their favor, but instead on the ability of the parties to weather the prohibitively expensive pretrial storms and on the good fortune of drawing a jury sympathetic to them. When the parties come to feel like victims, regard the lawyers as the only winners and believe that our legal system is only a game in which the merits are secondary at best and meaningless at worst, the legal system is in trouble. No system of justice can long survive when its central participants and intended beneficiaries—the parties and the public at large—lack confidence in, and respect for, that system and its representatives. We lawyers, as trustees of this legal system, must do our part to end this cycle of inefficiency, injustice, and cynicism.

Many believe that the answer lies in the state and federal appellate courts. They would suggest that the courts should recognize that our system is being corrupted by this "legal extortion" and should therefore eliminate or cut back on the availability of the expansive tort remedies which are the subject of abuse. Many see an encouraging trend⁴ in recent appellate decisions and legislative amendments.

For example, in *Dyna-Med, Inc. v. Fair Employment & Housing Commission*,⁵ the California Supreme Court openly criticized punitive damages for the first time in recent years. In that case, the court limited the availability of punitive damages in administrative proceedings. Recently, the United States Supreme Court heard argument in a case in which an award of punitive damages is being challenged as violative of the due process clause and excessive fines clause of the Eighth Amendment.⁶ Also in 1988, the California Legislature addressed the punitive damages issue by amending Civil

4. "Fortunately, the tide seems to be turning." *Oki America*, 872 F.2d at 316.

5. 43 Cal. 3d 1379, 743 P.2d 1323, 241 Cal. Rptr. 67 (1987).

6. *Kelco Disposal v. Browning-Ferris Indus., Inc.*, 845 F.2d 404 (2d Cir.), cert. granted, 109 S. Ct. 527 (1988).

Code sections 3294 and 3295.⁷ The most significant amendment to those statutes appears in the move from a "preponderance of the evidence" standard of proof to one requiring "clear and convincing evidence that the defendant has been guilty of oppression, fraud, or malice."⁸ The statute now also substantially limits pretrial discovery relating to punitive damages, prohibits plaintiffs from stating in the complaint the amount of punitive damages that are sought, and allows for a bifurcated trial, in which the defendant's financial condition is not presented to the jury until after liability has been established.⁹

On December 29, 1988, the California Supreme Court decided the landmark case of *Foley v. Interactive Data Corp.*,¹⁰ a wrongful termination lawsuit. In *Foley*, the court abolished all tort remedies—including damages for pain and suffering and punitive damages—for claims of breach of the covenant of good faith and fair dealing in an employment context.

Allegations of breach of fiduciary duty are being met with skepticism of late. In *C. Pappas & Co. v. E. & J. Gallo Winery*,¹¹ the Ninth Circuit held that when the parties' dealings are intended to give rise to mutual profits, there is no fiduciary relationship as a matter of law. The result is that in an ordinary contractual relationship, no fiduciary duty arises.¹²

With respect to claims of unfair competition under Business and Professions Code section 17200, the Ninth Circuit has recently held that there is no private right of action for damages.¹³

Another important example embodying this recent trend is the claim of emotional distress, a claim that can be conjured up in almost any situation. Here, courts have required plaintiffs to plead specific facts showing the offending conduct to be truly extreme and outrageous.¹⁴ Ordinary commercial disputes rarely, if ever, rise to this level. Moreover, serious foreseeable emotional harm must be demon-

7. Amended Stats 1987, ch. 1498, § 5 (Senate Bill 241).

8. CAL. CIV. CODE § 3294(a) (West 1989).

9. *Id.* at 3295.

10. 47 Cal. 3d 654, 765 P.2d 373, 254 Cal. Rptr. 211 (1988).

11. 610 F. Supp. 662, 667 (E.D. Cal. 1985), *aff'd*, 801 F.2d 399 (9th Cir. 1986).

12. *Richel v. Schwinn Bicycle Co.*, 144 Cal. App. 3d 648, 192 Cal. Rptr. 732 (1983).

13. *Little Oil Co., Inc. v. Atlantic Richfield Co.*, 852 F.2d 441, 445 (9th Cir. 1988); *accord* *Dean Whittier Reynolds v. Abascal*, Cal. Ct. of Appeals (#A04415), First Appellate District, Division Two, Slip Opinion 22-23 (July 21, 1989).

14. *See, e.g., Davidson v. City of Westminster*, 32 Cal. 3d 197, 649 P.2d 894, 185 Cal. Rptr. 252 (1982).

strated,¹⁵ and serious emotional distress is generally not foreseeable in an ordinary business situation.

Finally, in the area of promissory fraud the California Supreme Court, in *Tenzer v. Superscope*,¹⁶ has made it clear that nonperformance alone is insufficient to support an inference of fraudulent intent. The court stated that "if plaintiff adduces no further evidence of fraudulent intent than proof of nonperformance of an oral promise, he will never reach a jury."¹⁷

This author shares some enthusiasm for these developments. However, the reader should be dissuaded from believing that these limitations will solve the entire problem. First, neither the courts nor the Legislature should go so far as to cut off legitimate tort claims, thus leaving real victims without remedies. Second, a zealous advocate will always find a way to apply a legitimate tort principle to his case, whether justified by the facts or not. Third, these limiting legal principles are not self-executing; judges and juries must be entrusted with their application.

The solution, therefore, cannot lie exclusively in a set of bright line restrictions on the applicability of certain tort claims. Rather, we must encourage trial judges to do what they are paid to do—which is to apply the law, not pass the buck. Trial judges "are not referees at prize fights but functionaries of justice."¹⁸ As such, they must exercise their judgment and make the tough calls. The sooner in the process their judgment is exercised, the better. When the master calendar law and motion judge passes the buck to the trial judge, or when the trial judge passes the buck to the jury, they unnecessarily prolong the process, adding to the already exorbitant cost of litigation and frustration of the participants. Justice Frankfurter put it bluntly when he wrote:

The easy but timid way out for a trial judge is to leave all cases tried to a jury for jury determination, but in so doing he fails in his duty to take a case from the jury when the evidence would not warrant a verdict by it. *A timid judge, like a biased judge, is intrinsically a lawless judge.*¹⁹

Of course, the responsibility does not begin and end with trial

15. See, e.g., *Edwards v. Chain, Younger, Jameson, Lennucchi & Noriega*, 191 Cal. App. 3d 515, 236 Cal. Rptr. 465 (1987).

16. 39 Cal. 3d 18, 702 P.2d 212, 216 Cal. Rptr. 130 (1985).

17. *Id.* at 31, 702 P.2d at 219, 216 Cal. Rptr. at 137.

18. *Johnson v. United States*, 333 U.S. 46, 54 (1948) (Frankfurter, J., dissenting).

19. *Wilkerson v. McCarthy*, 336 U.S. 53, 65 (1949) (Frankfurter, J., concurring) (emphasis added).

judges. In order to encourage responsible and vigorous pre-trial screening of unmeritorious claims, appellate judges must defer to decisions of trial judges to dismiss claims at the pleading stage or enter summary judgment against unmeritorious claims. The trend in federal court toward the elimination of these specious claims at the pleading stage or at the summary judgment stage must continue. We must remember that while every man is entitled to his day (a decade for some) in court, he is not necessarily entitled to it before a jury. Such an improved pre-trial motion practice will of course not result in the pre-trial dismissal of every unmeritorious complaint. However, it will eliminate from lawsuits those claims that are unsupported by the law or for which the claimant cannot marshal significant factual support. This pre-trial judicial sharpening of the issues will allow the parties to devote their time, energy, and resources to the resolution of cases on the merits of their disputes and pursuant to rules they can understand and respect.

In order to accomplish such a marked improvement in pre-trial motion practice, it is not necessary to adopt wholesale rule changes at either the federal or state level. First and foremost, we need to change the attitudes of both trial and appellate judges. Law and motion judges should not be encouraged to pass the buck to trial judges, nor trial judges to juries. Appellate courts could help by paying more deference to the informed judgment of the trial court judges regarding demurrers and summary judgment orders. Second, the effectiveness of this expedited adjudicatory process would be enhanced if the Federal Rules of Civil Procedure were amended to extend the Rule 9(b) particularity requirement (and we should do the same for the state court analogue) beyond cases involving fraud to include punitive damages and their underlying tort claims. Third, the master calendar system in state courts should be modified to facilitate single assignments on major cases and state court judges should be provided with more research assistance. Fourth, and most importantly, the courts' conservative approach to summary judgment in state court must be dramatically altered. As noted below, this essay suggests that this can be done without altering the summary judgment statute.

Although the summary judgment statute does not so require, state courts routinely deny motions for summary judgment while conceding that the plaintiff has little chance of prevailing at trial.²⁰

20. See, e.g., *Slaughter v. Legal Process & Courier Serv.*, 162 Cal. App. 3d 1236, 1250, 209 Cal. Rptr. 189, 197 (1984) (noting with respect to issue of damages that "this evidence is arguably scant" where sole evidence consisted of plaintiff's statement that he "was, you know, upset" and "worried about not knowing where [he] was going to live"); *Zimmerman v. Stotter*,

Such rulings too often lead defendants—particularly in multiple defendant cases—to incur hundreds of thousands, or millions of dollars in fees defending claims the plaintiff should have little prospect of winning.

The federal summary judgment standards recently articulated by the Supreme Court in *Anderson v. Liberty Lobby, Inc.*,²¹ *Celotex Corp. v. Catrett*,²² and *Matsushita Electric Industrial Co., Ltd. v. Zenith Radio Corp.*,²³ if applied in state courts as in federal courts, would make a considerable contribution to the preservation of the integrity of our state court system. These standards are easily summarized. First, the moving party bears the initial burden of “‘showing’—that is, pointing out to the District Court—that there is an absence of evidence to support the non-moving party’s case.”²⁴ The burden is then on the non-moving party to show that there is a “genuine” dispute of material fact, i.e., that “the record taken as a whole could . . . lead a rational trier of fact to find for the non-moving party.”²⁵ Second, the inherent implausibility of the party’s claim is considered in determining whether summary judgment is appropriate: if “the factual context renders respondent’s claim inherently implausible—if the claim is one that simply makes no economic sense—respondents must come forward with more persuasive evidence . . . than would otherwise be necessary.”²⁶ Finally, if the evidentiary standard at trial requires “clear and convincing” evidence, then “the trial judge’s summary judgment inquiry as to whether a genuine issue exists will be whether the evidence presented is such that a jury *applying that evidentiary standard* could reasonably find for either the plaintiff or the defendant.”²⁷

These standards are not incompatible with existing California law, at least not as it exists in statutory form. Most importantly, California Code of Civil Procedure section 437(c) requires that a motion for summary judgment “be granted if all the papers submit-

160 Cal. App. 3d 1067, 1080, 207 Cal. Rptr. 108, 117 (1984) (admitting that plaintiff’s “instant action is tenuous at best”); *Joseph Schlitz Brewing Co. v. Downey Distrib.*, 109 Cal. App. 3d 908, 918-19, 167 Cal. Rptr. 510, 516 (1980) (admitting that “possible inference of fraud and conspiracy . . . gleaned from some of the allegations of the *Scheck* declaration” was “somewhat weak”).

21. 477 U.S. 242 (1986).

22. 477 U.S. 317 (1986).

23. 475 U.S. 574 (1986).

24. *Celotex*, 477 U.S. at 325.

25. *Matsushita*, 475 U.S. at 587.

26. *Id.* See also *United States v. King Features Entertainment, Inc.*, 843 F.2d 394, 398-99 (9th Cir. 1988).

27. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 255 (1986) (emphasis added).

ted show that there is no triable issue as to any material fact." This is functionally equivalent to the standard set forth in Federal Rule of Civil Procedure 56(c). There the language requires "no genuine issue as to any material fact."²⁸

The basic procedural and evidentiary rules do not vary significantly between the two systems. California Code of Civil Procedure section 437(c) places the initial burden upon the moving party, requiring that party to support its motion with "affidavits, declarations, admissions, answers to interrogatories, depositions and matters of which judicial notice shall or may be taken." Once the moving party has made a showing sufficient to sustain a judgment in his favor, however, the non-moving party "has the burden of showing that triable issues of fact exist."²⁹ The California statutory framework, therefore, presents no insuperable obstacle to the implementation of *Matsushita's* and *Celotex's* standards in our state courts.

The crucial issue, obviously, is the willingness of the federal courts under *Matsushita* and its progeny to grant summary judgment when the non-moving party has some evidence in his favor, though clearly not enough to convince a rational trier of fact. As we have seen, California courts often balk at this step, deeming the slightest perceived conflict in the evidence as raising a "triable" issue of fact. Nowhere in the statute is this result required, and it is not supported by the policies underlying the summary judgment statute.

The California courts have on occasion taken a more balanced approach:

The purpose of the summary judgment procedure is to discover, through the media of affidavits, whether the parties possess evidence which demands the analysis of trial. The object of the proceeding is to discover proof. A summary judgment will stand if the supporting affidavits state facts sufficient to sustain a judgment and the counter affidavits do not proffer competent *and sufficient* evidence to present a triable issue of fact. [citations omitted].³⁰

28. Both systems require that the disputed fact be "material." "Material fact" refers to a fact which, if proved, would change the outcome of the suit. *Compare Anderson*, 477 U.S. at 248 with *Oxford v. Signal Oil & Gas Co.*, 12 Cal. App. 3d 403, 410, 90 Cal. Rptr. 700, 704 (1970) (designating as material those facts which "could change the result one way or the other if resolved in favor of one side or the other").

29. *Chern v. Bank of America*, 15 Cal. 3d 866, 873, 544 P.2d 1310, 1315, 127 Cal. Rptr. 110, 114, (1976); *Michael R. v. Jeffrey B.*, 158 Cal. App. 3d 1059, 1065, 205 Cal. Rptr. 312, 317 (1984).

30. *Goldstein v. Hoffman*, 213 Cal. App. 2d 803, 810, 29 Cal. Rptr. 334, 339 (1963) (citing *Burke v. Hibernia Bank*, 186 Cal. App. 2d 739, 744, 9 Cal. Rptr. 890, 893 (1960);

More recently, the California Supreme Court has admonished trial courts not to "sap the summary judgment procedure of its effectiveness in cases wherein the party against whom the procedure is directed seeks to screen the lack of triable factual issues behind adept pleading."³¹ The court stated,

Summary judgment is proper only if the affidavits in support of the moving party would be sufficient to sustain a judgment in his favor and his opponent does not by affidavit show *such facts as may be deemed by the judge hearing the motion sufficient to present a triable issue*. The aim of the procedure is to discover, through the media of affidavits, whether the parties possess evidence requiring the weighing procedures of a trial.³²

The courts should recognize that the "weighing procedures of a trial" are simply not required where one party's evidence is clearly insufficient to convince a rational trier of fact, such as where a party's claim is rendered inherently implausible by the factual context in which it arises.

While consistent with the current statute, these recommended changes undeniably represent a substantial change in state court practice. They require, above all, a fundamental shift in the attitude of our courts with respect to the proper role of the judiciary in identifying and eliminating insufficient claims in pretrial proceedings. Nevertheless, this author suggests that such changes in approach are necessary for the legal process to function as it was intended and if we are to restore the public's confidence in that process.

It is possible to develop a tort system that treats plaintiffs fairly without coercing defendants into the intolerable choice between paying ransom or spending obscene amounts defending factually weak and inherently implausible claims. If more judges were to heed Justice Frankfurter's admonitions about the proper role of judges and were to thoughtfully use the tools readily at their disposal, the integrity and credibility of our legal system would be vastly enhanced. The public would have more respect for the law and its representatives and we could all spend our energy and resources resolving legitimate disputes, of which there will always be plenty.

Kramer v. Barnes, 212 Cal. App. 2d 440, 445, 27 Cal. Rptr. 895, 898 (1963). See also CAL. CIV. PROC. CODE § 437(c).

31. D'Amico v. Board of Medical Examiners, 11 Cal. 3d 1, 20, 520 P.2d 10, 25, 112 Cal. Rptr. 786, 520 (1974).

32. *Id.* (emphasis added).

B. *Transcript—High Technology Tort Litigation*

1. *Introduction—Professor Howard C. Anawalt**

I want to welcome you back to our session here on *The Future of Tort Litigation in California*. This afternoon our panelists will shift our focus of attention to the area of high technology torts, specifically, the problems that crop up in a vibrant economy such as ours in Silicon Valley and the special types of issues in context that come with a high technology development area such as ours and in the state in general.

I'd like to introduce and welcome our panelists this afternoon: Ron Malone, Lois Abraham, Judge Ingram and Peter Choy. We are very pleased to have them come and share their understanding and knowledge with us this afternoon.

This afternoon we will have a slightly different format from our sessions this morning and we will encourage you to ask questions at any time. We are eager to have you participate in our discussion. Ron Malone will address remarks to a proposed cure for high technology and tort abuse which corresponds to his paper by that same name in your pamphlet. Next, Lois Abraham is going to address problems of preliminary injunctive relief in high technology litigation, and then we will have a panel discussion and hash out some of the questions that have come up. Thereafter, Peter Choy has designed some hypothetical problems that closely mirror the realities of the situations that will come up predictably in high technology industrial situations. Throughout this discussion Judge Ingram will keep a watchful eye on us to alert us to the things that have come to his attention through long experience, originally as a trial lawyer, and then on the superior court bench and now on the federal bench in our district of California federal court.

I would like to introduce our topic by reading one of Mr. Choy's hypotheticals:

The Vice-President of marketing has resigned from his company and will start next week as the Vice-President of sales and marketing at a company which is viewed as one of your company's top competitors. The Vice-President is privy to all the planning documents and has just participated, only three months ago, in formulating your five year plan, your strategic

* Professor of Law at Santa Clara University School of Law; director of Santa Clara University School of Law's Summer Law Program in Japan 1984-1987; J.D., 1964, University of California, Berkeley; author of *Ideas in the Workplace: Planning for Protection* (1987).

marketing plan and plan for the next calendar year.

He has been with the company for four years. In his first two years he was director of customer marketing. His responsibility at that time was care and feeding of your company's, Galaxy's, one-hundred largest accounts. He has been in his present job for two years. When Galaxy hired him he was director of customer marketing at a mainframe computer company.

The Vice-President of marketing is a very charismatic fellow and has been responsible for hiring several talented individuals into the company. From outward appearances many of them have great personal loyalty to him. This departing employee refused to sign any affirmation of his confidentiality agreement when he left. You noted that he took his Rolodex file with him.

All right Ron, please give us your ideas.

2. *The Panelists' Discussion**

a. *Ronald Malone*

At the risk of exposing myself as a cynical defense lawyer, I have agreed to come here today to share with you some of my observations about what I regard as some serious short-comings in our tort system and to propose some improvements. If what follows sounds to some of you like an attack on plaintiffs lawyers or on judges, I apologize in advance because this is really intended to be a critique of the system; not of individuals. Insofar as individuals are concerned, we all are part of the system and I believe that we all are influenced by that system in the manner in which we behave. So my comments really are not intended to be personal, but systemic.

With that let me get right to the theme of my paper, a copy of which is in your materials. And that is that California tort law is often a tool of oppression rather than an instrument of justice. This is true in many areas, not the least of which is the high technology area where the technical aspects of those cases and the amorphous legal issues combine with a widespread fear of unpredictable juries and runaway damage awards to make the litigation process obscenely expensive. Ever-expanding and omni-present tort concepts, including statutorily based causes of action such as misappropriation of trade secrets and unfair competition, are the subject of widespread misuse.

Tort claims such as promissory fraud, breach of fiduciary duty,

* We are indebted to Professor Howard Anawalt for moderating this discussion.

tortious breach of the implied covenant of good faith and fair dealing, bad faith denial of contract, interference with contractual relations or perspective economic advantage and their concomitant claims for punitive damages are injected routinely in virtually every ordinary commercial contract dispute. They are often injected with woefully little factual justification as a means of increasing economic leverage where the underlying contractual relationship does not provide it, and as a means of increasing damage exposure.

In short, tort claims in the commercial context, not always but often, are used as a means of extorting settlements. Once he or she is informed of the rules of the game, what prudent Silicon Valley executive—no matter what the merits of the case—wants to bear the enormous burden of attorneys fees, of expert witness fees, of court costs, of lost management time, just to face the incredible uncertainty of a jury trial—particularly a jury trial with the potential of virtually unlimited punitive damages awarded against him? Why not just settle?

Of course the early settlement of legitimate disputes should be encouraged. But the settlement of cases irrespective of their merits and out of fear of the high cost of battle or the fear of unpredictable juries and their sometimes runaway damage awards, feels to the settling defendant more like making an extortion payment than settling a lawsuit. That is not good for the system. It causes disrespect for the law and its representatives and ultimately it breeds lawlessness itself because that kind of conduct will be repeated and imitated by others.

To put this in context just a little bit let's think of two or three scenarios that typically arise in the high technology context in the Silicon Valley. The first is spin-offs and start-ups. In Silicon Valley there are probably more start-up, emerging and spin-off companies than any place on the planet. Engineers move from company to company. A lot of people believe that this kind of cross-fertilization of ideas is one of the great engines of innovation and something that should be encouraged. Sometimes when engineers leave one company to start-up another, they found their new venture on a corporate opportunity that they misappropriated from their previous employer and sometimes they do it on the basis on stolen trade secrets. When they do that, they are justifiably the subject of vigorous prosecution by the previous employer.

Frequently, however, it's not quite that simple. Rather, even before the previous employer knows for certain that any trade secrets were taken or that they are likely to be used in the competing ven-

ture, the employer immediately files a pre-emptive trade secret lawsuit. The mentality often times in this context is "sue first and ask questions later." Sometimes there is some merit to these cases and sometimes there is not. Virtually always, there are ulterior motives on the part of the plaintiff. Those include interfering with the financing of the start-up, disrupting and distracting the management of the start-up, extending the new competitor's time to market, that is delaying new product releases, and reassuring or intimidating the plaintiff's loyal, that is, non-departing employees.

A blameless defendant in this kind of situation can choose to fight if he's got vast amounts of extra, unneeded capital. He can even file a cross-complaint. Typically however, that's not what happens. What happens is that these cases get settled and settled very quickly. Typical types of settlement terms include a nominal payment by the defendant, the amount of which would be confidential and secret; perhaps an agreement to be subjected to a technological audit by third party consultants, and most importantly from the plaintiff's point of view, is an agreement not to hire any more of its employees.

Another scenario that we see coming up time and time again in Silicon Valley, particularly as emerging companies mature, is a lawsuit by the founder of the company against his own company after he loses control. The dream of these founders is to start their own companies. They envision themselves going public. In order to go public they need to raise additional capital for expansion. They do this typically through venture capitalists. Venture capitalists come on to the board and as the company becomes more and more profitable, as its sales grow to maybe 25 million dollars a year, the venture capitalists envision someone other than the founder as the CEO to take this maturing, about-to-be-public company into the future. As that founder is eased aside or upstairs to make room for stronger management, he loses confidence in the venture and he becomes dissatisfied. If the business runs into problems and does not go public as planned, the fur will fly and a lawsuit will almost inevitably follow.

That founder may have a legitimate lawsuit. He may have had a written employment contract which was breached when he was terminated or eased aside. Does he sue for breach of the written employment agreement? Yes, but there will also be the obligatory causes of action for breach of oral promises and implied-in-fact contracts. But he will not stop there, it never does. He will add tort claims for a breach of the implied covenant of good faith and fair dealing and for interference with prospective economic advantage. Does he sue only the company? No, he will sue the directors and for

symmetry's sake, a smattering of officers, knowing full well that his leverage against the company will be increased because of the scarcity of directors and officers liability insurance.

The kind of allegations that he will throw in include: promissory fraud, for example, against the venture capitalist for not disclosing its secret intent, harbored at the time of the initial investment, to sack the founder and replace him with a Harvard MBA type who will subsequently ruin the company; a conspiracy by all of the directors and some of the shareholders to breach various and sundry alleged fiduciary duties. And just to be sure of the unavailability of the business judgment defense, he will throw in an allegation that his former colleagues, now known as conspirators, all acted or voted with corrupt or venal purposes.

One final example is the typical dispute between software companies. There is a written contract that governs the performance of both parties. Things do not work out, the product is not marketed as intended, it is not developed as intended, and somebody loses some money. You have the makings of a breach of contract lawsuit. Well, do they sue only for breach of contract? Of course not. You will see the implied covenant and good faith and fair dealing, bad faith denial of contract and a breach of fiduciary duty. These are typically people negotiating at arm's length, but when things go bad, suddenly there is a breach of fiduciary duty, again the predicate for punitive damages. The typical kinds of allegations would be that the one party had superior knowledge and bargaining position, the plaintiff relied on the other party. There will also be perhaps interference with prospective economic advantage, and maybe a little promissory fraud to spice things up.

Now all of this is done with a cold cynicism on the part of the lawyers. They know that the name of the game is to plead enough to keep the trial judge from sustaining a demurrer without leave to amend or granting a motion to dismiss with prejudice. They know that Rule 11 and CCP 128.5 are no real threat to them if they are at all artful. They know that abuse of process and malicious prosecution exposure are difficult for claimants to establish, are far off and, most importantly, they can be dealt with at the settlement stage.

After the plaintiff has overcome these pleading hurdles, discovery is conducted with a keen awareness that summary judgment against them on the tort claims is to be avoided at all costs. They know that typically, particularly in state court, that simply pointing to some conflict in the evidence, no matter how insubstantial that conflict is, will be enough to deny summary judgment and put the

case before a jury where who knows what will happen. Thus, we see that plaintiffs typically or frequently append weak but artfully-pleaded tort claims to their contract claims with the hope that they will find some factual support for those tort claims during discovery. But that is only their hope. What they know is that the name of the game is to prevent the defendant from getting summary judgment and if you are successful in preventing summary judgment until the eve of trial, you have the hope and expectation of settling the contract claims for more than they are worth. And what's wrong with this? This is just lawyering, isn't it?

It is a real tragedy when this kind of situation occurs. What happens right before trial, even a couple of months before trial, is that because of the complex nature of the cases and because of the fear of defense counsel of punitive damages and tort liability, both sides have invested more in attorney fees and expert witness fees than the contract claims are worth. When the process breaks down this way, the result is unhappy clients and wealthy lawyers. But when the parties feel like victims, when they regard the lawyers as the only winners and when they believe that the legal process is a game where the merits are secondary at best or meaningless at worst, you have a legal system that is in serious trouble.

We lawyers are guardians of the legal system and we have an opportunity and the responsibility to do something about this situation. But what can we do about it? Some believe, as we heard on the panels this morning, that the answer is for appellate courts, both at the state and federal level, to recognize that the system is being corrupted by this kind of legal extortion and to cut back on the availability of these expansive kinds of torts. Many see a very, very, encouraging trend in these recent appellate court decisions and legislative amendments.

Just briefly, in the area of punitive damages, the California Supreme Court in 1987, for the first time in recent past, was openly critical of punitive damages and refused to extend their availability into the administrative area. The United States Supreme Court, as was mentioned earlier, has granted *certiorari* in a case challenging the constitutionality of punitive damages. The California Legislature last year amended the Civil Code provisions relating to the procedural availability of punitive damages by requiring clear and convincing proof, limiting discovery and allowing for a bifurcated trial.

Probably most importantly along this line is the *Foley* decision of the California Supreme Court in late December of last year, which eliminated tort damages for breach of the implied covenant of

good faith and fair dealing. That was in the employment context, but I think, as Justice Kaufman suggested, the analysis of the court would extend beyond the employment context.

Similarly, breach of fiduciary duty allegations and contentions are being met with skepticism of late. In situations where you have a commercial contract where each side is seeking profits for themselves, the courts have held as a matter of law that there can be no fiduciary relationship. In the unfair competition area, the Ninth Circuit recently held that there is no private right of action for damages for Business and Professions Code section 17200 Unfair Competition Claims. Courts are limiting the availability of emotional distress in the commercial context. Promissory fraud is being viewed with skepticism. The California Supreme Court, in 1985, held that non-performance alone is not enough to support an inference of fraudulent intent at the time the promise was made.

Is this the answer to the kinds of problems to which I have alluded? I think that these kinds of cutbacks are helpful, but in my view they are not the answer to the kinds of abuse to which we have discussed. This is true for several reasons. First, the courts and the legislature cannot go too far in restricting the availability of these kinds of torts without cutting off legitimate tort claims and leaving real victims without remedies. We cannot have that, of course.

Second, no matter what the law is at the appellate level, zealous advocates will do their level best to find a way to apply a legitimate tort principle to the facts of their case, whether the facts really justify it or not.

Third, and most importantly, these limiting principles that are propagated by the appellate courts are not self-executing; a judge or jury must implement them.

The answer, therefore, cannot lie exclusively in these kinds of bright line limitations, whether imposed by the legislature or by the courts. Rather, I submit, we must encourage trial judges to do what they are paid to do, which is to apply the law, not pass the buck. Justice Frankfurter said, "trial judges are not referees at prize fights, but functionaries of justice" and as such their job is to exercise their judgment and to apply their judgment to the facts before them. The sooner in the process they do that, the better we will all be. When the state court master calendar law and motion judge passes the buck to the trial judge and refuses to rule on a demurrer or on a motion for summary judgment, or when the trial judge passes the buck to the jury, they unnecessarily prolong the process, add to the already exorbitant cost of litigation, and frustrate the participants. Again

Justice Frankfurter put it bluntly when he said, "a timid judge, like a biased judge, is intrinsically a lawless judge." But of course the responsibility cannot begin and end with trial judges.

Appellate judges must defer to the judgment of trial judges when they sustain demurrers, grant motions to dismiss, or grant motions for summary judgment. In federal court, there is a growing trend to cut specious claims off at the pleading stage, and more importantly at the summary judgment stage. We must remember that while every man is entitled to his day, some say decade, in court, he is not necessarily entitled to it before a jury. In order to accomplish the kind of improved judicial pre-trial sharpening of the issues to which I allude, we do not need to make wholesale rule changes at either the federal or state level.

First, and foremost, we need to change the attitude of trial judges and appellate judges and have them exercise the judgment and the powers that they have. Second, on the rule change side, if we could amend Rule 9b and extend the particularity requirement at the pleading stage beyond fraud but extend it to punitive damages, it would make the task of the trial judges at the pleading stage much, much easier. Third, on the state court side, serious consideration should be given to modifying the master calender system and/or to encouraging single assignments on major cases, and to providing state court judges with more research assistance. Fourth and, perhaps most importantly, we have to change the ultra-conservative approach to summary judgment, particularly in state court but also sometimes in federal court, that is being followed by many judges.

The summary judgment standards recently articulated by the United States Supreme Court in the *Anderson*, *Celotex*, and *Matsushita* cases are the answer, I think, to our problems in both federal court and state court. Let me briefly summarize what are those standards. First, in the summary judgment context, again in federal court, once the moving party makes his prima facie showing, that there is an absence of evidence to support the non-moving party's case, then the burden shifts to the non-moving party to show that there is a genuine dispute of material fact. That is that the record taken as a whole could lead a rational trier of fact to find for the non-moving party. Second, and this is perhaps the most important one, the inherent implausibility of a party's claim should be considered in determining whether summary judgment should be entered, that is, whether there is a genuine issue of material fact. And finally, if the evidentiary standard at trial is an enhanced one, such as clear and convincing proof, the trial judge should take that enhanced stan-

dard of proof into account when ruling on summary judgment.

Now these standards are federal standards but they are not inconsistent with the California statute. The key language of the California statute, section 437(c), is that there is "no triable issue as to a material fact." If there is no triable issue, summary judgment is entered. The comparable federal standard is "no genuine issue of material fact." Materiality is defined the same in both contexts. Indeed, the Supreme Court in *Celotex* used "genuine issue" and "triable issue" interchangeably. So there really is no functional difference in the federal statute and the state statute.

California courts have long-rejected the old scintilla of evidence approach which, as you will recall, simply meant that in the directed verdict context or the summary judgment context, if the non-moving party could point to even a scintilla of evidence, some shred of evidence that the jury might consider in opposition to the overwhelming weight of contrary evidence, then the judge would have to deny the motion for a directed verdict and let the case go to the jury. That approach has been rejected in California and in the federal courts. As the paper pointed out, there are hints in the California appellate cases that in determining whether a triable issue of material fact exists, the trial court should exercise some judgment and examine the substantiality of the conflicting evidence.

If that is true, in a nut shell, our problem is not so much with the summary judgment rules but the manner in which we apply them. I think the problem is that state court judges particularly, but also federal judges to a lesser extent, end their analysis when they see any conflict in the evidence, once they see that there is some evidence in opposition on a material issue, and their reflexive response is to deny the motion. Denying the motion is the safe thing to do because appellate courts do not reverse summary judgment denials as often as summary judgment entries. At least that has been the apparent pattern.

I submit that all we have to do to vastly improve the system is to take the process half a step farther. When a judge sees that there is a conflict in the evidence, the analysis should not stop, but that judge should move on to examine that conflicting evidence and determine the substantiality of that evidence and then make the hard decision as to whether the conflicting evidence is substantial enough for a reasonable trier of fact to find for the non-moving party. I think that is really the law in federal court and even in state court. Put bluntly, if the evidence would not be sufficient to get by a motion for a directed verdict at trial, it is not or should not be, sufficient to get by a

motion for summary judgment before trial.

While these kinds of changes are consistent with the California summary judgment statute, they undeniably represent a substantial change in the way the state courts work. Notwithstanding that, I believe that unless we make this kind of a change, the legal process will not be regarded as functioning as it was intended to and the confidence of the public in our legal process will continue to erode. It is possible to have a tort system that is fair to plaintiffs without coercing defendants into making the intolerable choice of paying ransom or hundreds of thousands, if not millions of dollars, defending claims that are factually weak or inherently implausible, but nevertheless dangerous because they have punitive damages exposure and they are going to be before a jury. If more judges, both state and federal, heeded Justice Frankfurter's admonitions about the proper activist role of judges and fairly and thoughtfully applied the tools which are readily at their disposal, the integrity and the credibility of our legal system would be vastly enhanced. The public would have more respect for the system and for its representatives and we could all spend our time, our energy, and our resources resolving legitimate disputes of which there will never be a shortage.

b. *Lois Abraham**

You were reminded this morning that you are hearing from advocates. Most of us have a fairly consistent group of clients, a fairly consistent group of viewpoints that we press for them and that doesn't change in these conferences. Conferences have become a kind of lobbying ground in a lot of ways. Having warned you of that, and I will identify my bias, I most frequently represent plaintiffs in high technology lawsuits, the so-called protectionist side. That's the filter through which you probably should pass my remarks.

Having said that, there are lots of areas that I could not agree more with what Ron has said, mainly in the area of summary judgment. That's something that a lot of attention could go to. I do have a little trouble in viewing the system in the way it works in our area of high technology as a tool of oppression. That seems to me to be a bit overstated. I think it actually works pretty well, maybe not in the way that you see in the Federal Rules of Civil Procedure because a lot happens on the edges, but as far as the results and the protection

* Partner, Brown & Bain, Palo Alto, CA; member of Brown & Bain's management committee, specializing in high technology litigation; J.D., 1973, Arizona State University, College of Law.

of the interest involved, it isn't the worst system we could come up with. Maybe not the best, but not the worst.

The interests on either side of these cases are very strong. In terms of the economic interest you have the interest of the on-going enterprise which has developed technology, wants to keep it, wants to wring out the most profit from it. And, on the other side, you have the economic interest of the entrepreneur and the investors who want to go with that entrepreneur and create something different—two very strong economic interests frequently at battle.

There is also the policy, very strong in California, of protecting the worker's right to take his tool kit—his experience and his knowledge—and use that for the benefit of whomever he sees fit, his own or any employers. Another policy concern is the tension between standardization as a way of increasing the technology and innovation. The non-protectionist view can be articulated in a very rational way, and the reason it is rational is because there is a lot to it. You don't want to re-invent the wheel at every turn. You want to be able to build on what has gone before. On the other hand, innovation sometimes just doesn't happen that way. Very interesting in the industry right now, and in this valley, are the stories in the press about the challenge to the established technological giants such as Motorola and Intel, by such up-start companies as MIPS and SUN. They didn't do that building on with what had gone before so much as they did by jumping ahead, saying, "with what has happened in the last ten years, here's a much better way to go." Whether it's much better or not, it has certainly resulted in a burgeoning of technology, and a response by the former unchallenged leaders. So we have a lot of new things coming on and interests, very important and strong interests, that are at odds between the standardizers and the innovators. One thing that Ron said that is absolutely true, and particularly in the technology suit where you have employer/employee contention.

I am going to be focusing mainly on this conflict. But, it's not as simple as Ron suggests. The trusted high level employee walks out and the employer appears in your office. He wants to do something now! Right now! It is a little hard to even know at that early a stage what has happened. And it is true that when the employees leave to enter into a competitive business, former employers are usually concerned about the *threat* of misappropriation, rather than actual misappropriation. In some cases there has already been misappropriation and that is pretty easy. But how do you evaluate this threat that something bad is going to happen, something that the former em-

ployer wants very much to cut off as soon as he can, and rightly so. It is absolutely true that once a trade secret is out of the bag it's hard to put it back in again.

Perhaps very little has actually happened. Ron referred to ulterior motives in bringing suit, such as frightening other employees into not leaving, crushing financing, etc. Often times those are concomitant of what happens. That is all part of the action, that is all part of the scene. Nobody who understands how these things work could believe that the employer's reaction is always baseless. Often a group of technologists who have left a company are met at the front door of the company by the venture capitalists or whoever else is financing them. And they make a lot of promises in return for being funded. They have a business plan they have to meet. There are pressures on people who go out into start-ups. After the kind of "romantic time" when they get funded, there are huge pressures to make their plans. The people who were their former employers know that. They know with this kind of pressure and with the best will in the world, it is unrealistic to say, "They are just going to keep that little compartment of their brains where they have all our secrets closed under the face of these pressures." Well maybe they are. That's pretty hard to know at the front end.

If, in fact, the former employees will be doing precisely what they were doing in their old businesses, only either for themselves or for a new employer, in many states, although not in California, there is a presumption that it's not possible to keep all those secrets locked up. And they will be prohibited by injunction from starting up such employment. In California, we don't have that kind of a presumption. In some of my cases I wish we did. The law varies throughout the United States.

The area I think which can be greatly abused and which fortunately our judiciary in this area seems to be cognizant of, keeps a watch over, is the area of preliminary relief. What happens in the very short term is extremely important to all those interests that I described earlier.

And here you have another dichotomy. A temporary restraining order can be a vicious thing for a new little company. A preliminary injunction hearing on the other hand may be the best thing to happen because it offers an opportunity to get litigation and all the expenses that run with it cut off at a fairly early stage. But there is a dynamic that occurs that can work very harshly against the defendant in one of these situations. It starts when the plaintiff's attorney, and I'll plead guilty, runs into court with fifty pages of papers and

says, "We need immediate relief, immediate." Well you know that the papers have taken two weeks to get together anyway, so right there immediacy is a little suspect. And the other side, if this TRO hearing goes forward, has no time to respond to what's a fairly well orchestrated attack. That is dangerous, and in this valley, at least, I have never gotten away with it. On the other hand, I was just representing a defendant in Texas where my opposition had been able to get a temporary restraining order, totally unedited from the one he had proposed based on a complaint without declaration, the complaint verified by the outside attorney. So as you can see, standards around the country vary quite a bit.

Here I think the protection is pretty good at the front end. If, in fact, a preliminary injunction hearing is set with reasonable time for reasonable discovery on both sides, that can work to the benefit of both parties. The standard for preliminary injunction is fairly well articulated in general but not into the specifics. The standard is, if you've read these cases, a sliding scale. The better chance you have of winning on the merits, the less showing you must make on irreparable harm, but no matter how good your showing on the merits is, there must be what is called a significant threat of irreparable injury. Well what's a threat?

In the situation I described earlier, is that a threat? Is that the kind of a threat for which you should get preliminary injunctive relief? We have a trade secret statute in California and there is language in it that if there is actual or threatened misappropriation it may be enjoined. There have been cases which argued that that gives the court authority to grant an injunction on a lesser standard than the ordinary standard of harm. But the essential question is: is this the kind of threat of harm that the statute intended to protect?

There are a couple of things that come through from the cases here, and one is if you have a client who is planning to leave his company, you should tell him not to take any documents with him. That is not a good move. The overt theft of documents which are considered proprietary and which on their face show that they are very likely to be proprietary, is a fairly decent basis for preliminary injunction.

In other cases it is a little harder to assess the threat of harm. There are cases where concealment of the nature of the new employment has been considered sufficient threat of harm to justify an injunction. The insensitivity of the new employer to the fact that the former employee has trade secrets and shouldn't be put in a position where it would be almost impossible for him or her to fulfill his

employment duties without using and revealing them has been grounds for an injunction. And the disclosure of trade secrets before hand, which occasionally actually happens, has been sufficient grounds. If a company has a technological problem which it hasn't been able to resolve on its own and goes out and hires someone out of your company who has that solution, you may stand a pretty good chance of getting an injunction. If you are in a situation where your client has time to organize a case for a preliminary injunction or against a preliminary injunction, given the bench we have in this area and the precedents, contrary to this being a tool of oppression, I think it is a system which comes up frequently—and that is about all you can ask in a pretty imperfect world—with the right solution.

c. *Judge William Ingram**

First of all, I would like to make an observation about where we happen to live. There is probably no place on the planet where there is more innovative work going on and where people change their places of employment so often. But just think how dismal that is in the history of American industry, where we all know the thirty, forty, fifty year men who work for a company. For example, everyday when I ride the train to commute I find this man who is a conductor. He says "I am number one. I have been here fifty years." Today, however, it is a whole new ballgame and everything that serves the community, including the courts, has got to acclimate to it.

I would like to address a number of comments on what has been said today, let us take summary judgment first. I do not think that in my fifteen years on the Superior Court bench anyone ever granted a motion for summary judgment. It was just one of those things. As a matter of fact, everyone considered a motion for summary judgment as a way to take a free deposition—everyone was required to file declarations—and that is how you found out what the other party's contentions were going to be. That was the beginning and the end of the benefit of a summary judgment motion.

On the court that I sit on now it is quite different. There are a couple of factors involved and I do not think any of them are a conscious desire or even a perception that the tort law is being abused. I do not think that is a "judicial" perception necessarily. What the

* Chief Justice of the United States District Court for the Northern District of California 1976-present; also served as Municipal and Superior Court judge in Santa Clara County; L.L.B., University of Louisville School of Law; member, American College of Trial Lawyers and the American Board of Trial Advocates.

courts are interested in is case management. We all know that a lot of dead wood gets filed and one way to get rid of the dead wood at the appropriate time is to grant motions for summary judgment. So I do not think that the district court bench needs very much acclimatization to being willing to grant summary judgments.

There are a couple of things that I noted, one is we have got to remember that no matter how we end up on a case, all the rules have to be strictly adhered to no matter how bad a case looks on first blush. Every intendment has to be given to the party opposing the motion for summary judgment. It bothers me when you are supposed to consider his version of the story inherently improbable. How much weighing of the credibility of witnesses, as an example, might go into the making of a determination like that. You cannot weight the evidence in that sense. What you are looking for is: does this side have enough to get past a non-suit or a motion for a directed verdict? You do not ask who is telling the truth, where the substantiality of the evidence is, or if there is enough, assuming the court or jury believes the admissible evidence, to get past the non-suit.

But you cannot get into weighing credibility, I wonder if you can even weigh the plausibility of a theory or a factual recitation. That is pretty interesting. In every other respect I think I agree with what Ron Malone said about what is the duty of a court. Justice Frankfurter put his finger right on it, that you do not fulfill your duty as a trial judge unless you do give people the relief to which, under the law, they are entitled. The Supreme Court, as indicated, has been very helpful to us in the last few years with the three cases that were just cited to you.

Now on to temporary relief. I cannot recite too much on trade secrets. My court seldom sees much about trade secrets unless it is attached to some intellectual property case that is seeking a concurrent type of relief of some sort. Maybe that is because I am not aware of any federal statute that protects trade secrets and unless there is a federal question that brings it in to us, or unless the parties are of diverse citizenship (which is unlikely if they are both in Silicon Valley) we are not going to see too many of those.

On preliminary relief, my court sees a lot of intellectual property cases in these types of companies we are talking about. Remember on a temporary restraining order (TRO), you do not even know the lawsuit is on file. Somebody hands you their ten inches of papers as you walk through the door to the judges office and there you are. Usually, in my court, preliminary application is handled in chambers and off the record and they are not granted very often. You are

only talking about a ten or fifteen or twenty day window in time. If you have what looks like it has something going for it in terms of urgency, but it is not enough to get a TRO, you can get a preliminary injunction hearing set quickly. Usually when both counsel are present they do not want hearings set quickly because they have to get ready for them.

However, in the case of TRO's, you must have a case, for example, where somebody wrote a letter to the customers of their former employer and told the recipients of the letter that they were prepared to give them the benefit of all the experience and the techniques that they got from their former employer. The harm has to be imminent and grave. The only time something like this might come up is where the "trade secret" at issue is not a customer list or some piece of technology and there is going to be a trade show on Saturday. The former employer shows up at five o'clock on Friday afternoon in my court and says that their former employee is going to display an item that incorporates all of their trade secrets. Whoever is trying to get the TRO better be able to tell the court exactly what the item is, but that still might not be enough. At least the court would try to accommodate the people and try to get them to stipulate to something and then give a reasonable protection one way or the other. However, these are real problems.

For example in a patent case, somebody comes in and says we need to have the infringement of our patent enjoined. As a preliminary question (I do not know the answer to this) is the presumption of validity of a duly issued patent sufficient to show a probability of success on the merits for preliminary relief alone? We all know that the presumption of validity can be overcome by showing that the patent was obvious, that it was anticipated, and that there is file wrapper estoppel. All these things apply, but to hold status quo is not enough. These are the sort of things that come up and we get them all the time. It is very seldom a week goes by where you do not get things like that.

d. *Peter Choy**

Well, I get to be the aggrieved plaintiff in this scenario, Howard, that you were kind enough to read at the outset of the session. And after listening to Ron's provocative and well articulated thesis

* Group General Counsel for Sun Microsystems, Inc., where his practice includes product development, licensing of technology and software, and intellectual property law: J.D., 1972, Yale Law School.

and then hearing consideration to the contrary presented by Lois, I am as confused as ever. I think what I would like to do is perhaps return to the scenario, if I may, and refresh our memories as to what the facts were and perhaps I could present my situation to counsel.

The Vice-President of marketing of my company has resigned and is starting work next week in the same capacity for our chief competitor. The three things that most concern us about this are that the Vice-President of marketing is privy to all of our strategic marketing and product planning secrets. He knows our customer list and was responsible for servicing our hundred largest accounts over the last four years. And also he is a very charismatic leader and many very talented employees in the company are loyal to him.

When he left he refused to sign any confirmation of the confidentiality agreement that he signed when he became an employee originally, and he took his office rolodex with him.

My management is very concerned that there is no way that he can perform his function in his new capacity as an employee of the new company without inevitably trading upon trade secret information that is proprietary to my company. The question is how can he possibly do his job at his new company without using things that belong to us. We are also very concerned that he'll exercise his very considerable personal charisma to hire away the employees at the old company who are loyal to him.

My question to counsel will be, have I been wronged? And if so, what's my remedy?

e. *Panel Discussion*

Lois Abraham

If I were the counsel on the other side of the telephone, the thoughts going through my head would be, "Oh, Oh." This is exactly the type of situation which is going to cause the most anguish and anger in the client. And this is very close to the type of situation which likely is not going to be the proper one to go after a temporary restraining order or maybe even preliminary injunction. Why? And I have not even talked to Peter yet but here's what's going through my mind.

You have one person leaving right now and that in itself is going to make it difficult to show that this is a horrible threat. He is not a technical person, the knowledge that he has is in the strategic

business areas. He knows the customers, but probably so does anybody who goes through and reads the trade journals, and he has not done anything yet that Peter has explained to me is against the law. Yes, he could take a few employees with him, that isn't against the law either, so I would kind of get into this easily with Peter by saying, "Peter, what are the goals, the objectives, that you'd like to try to obtain here. If you could tell me a little more about those then I will be able to tell you what I think are our options."

Peter Choy

Well I suppose the real fear of my management is that he is going to hire away these key people to his new company.

Lois Abraham

Well, that is kind of the system we have here. We don't usually keep balls and chains on our employees and if they want to go some place else they can. Now if your fear is that if you get a group of people at a new employer, you are going to be in much graver danger of losing your competitive business information and your trade secrets business information, particularly related to your strategic plans, where the company is going, and perhaps even to confidential personnel information about the salaries of some of the people that they might be interested in, what kind of stock options they had from you, what they are good at, now there we might be able to help you. But I have to tell you that I don't think we're going to be able to go in and make a big splash here by getting you a preliminary injunction right off the bat.

Peter, maybe we don't know enough about what's going on here and maybe what you need to do is tell me how the conversation went when your Vice President refused to sign his reaffirmation of his confidentiality agreement. Did he argue that the things that you were talking about weren't trade secrets? What was his rationale?

Peter Choy

Well he just refused to cooperate and stone-walled me, and it was very unpleasant. His whole demeanor suggested he was about to embark upon some activities antagonistic to our company, and we are very concerned about that.

Lois Abraham

I think you have every reason to be concerned, and I wish in this situation sometimes that we weren't in California because I could do more for you. But I tell you quite honestly that I think we are right close to the line here.

Peter Choy

Did I forget to mention that he is employed in our Massachusetts facility and our chief competitor is also a Massachusetts company?

Lois Abraham

I like this case better. I think that what we first want to find out is whether Massachusetts is a jurisdiction which has a presumption. Sounds to me like this fellow is going to be doing very close to the same thing for his new company as he is doing for you. We can find out if there is a presumption. If there is a presumption and strong case law, then I think you might want to file your complaint, try to get expedited discovery to find out exactly what he will be doing, and we'll get a preliminary injunction motion on to see if it turns out that he is going to be operating in the same capacity. It may be that there is going to be inevitable disclosure of your trade secret information and we can do something about it. But, as far as coming in and waving TRO papers, this just does not happen, Peter.

Professor Howard Anawalt

Lois, let me ask you a couple of questions about that last response. When you say that it sounds like this employee may be doing the same thing, how much are you going to lean on Peter to give you some strong information about what the trade secrets are that may disappear, or what it is that's going to go with him, because certainly he can go be a director of marketing somewhere can't he?

Lois Abraham

The trade secrets that Peter and I would have to rely on are the strategic business plans, the plans for activity over the next year. I don't think there is any doubt that a competitor would love to have the strategic business plan of its main competitor and know where it was going in the next year.

Judge Ingram

Well do all these things apply if he goes any place in the industry or only if he goes to the competitor? Does that make a big difference?

Lois Abraham

It makes some difference because it leads to this theory of inevitable disclosure and harm. The harm, if he is going off to a company with six employees with sales of \$250,000, is not quite so immediate or inevitable.

If during a conversation, the exit interview, the ex-employee or the about to be ex-employee, exhibits the attitude "Well none of this is trade secrets, I don't know any trade secrets, nothing I know isn't in the public domain," I think that is a basis for a reasonable apprehension on the part of the employer. The first thing that he is going to do when he gets in his new job is tell everybody all that. A refusal to sign might be based on the fact that his lawyers told him don't sign anything. But if that goes further and it becomes a rejection of the concept that anything that he takes with him is proprietary to the company. I think it is useful for Peter's case.

Professor Howard Anawalt

I am sitting down here at the other end of the table imagining myself to be a clever Vice-President of marketing and I am about ready to leave, just as you said. I have also been listening to the other descriptions of the legal process here and I get the distinct impression that it is something that I would call "non-legal" pressures that hang over my head if I want to leave a company.

For example, if my attorney succeeds in winning and prevents me from being subject to a preliminary restraining order, or preliminary injunction, I still go home and worry about the fact that the case is still on the judge's calendar in the future sometime. Do I have the wrong impression as a person that looks at this system? A non-legal person.

Lois Abraham

Well I don't know whether the case hangs on forever. But no, you are accurate. This becomes kind of a risky business for you because you are on the line. Can you, as this clever Vice-President of marketing, really draw a line and say, "I do know some information

but I will never use it." How do you ever know when you are using it?

Professor Howard Anawalt

Well that is just it. That is that ball and chain you said we did not have.

Lois Abraham

No, I think what it is is the true tension of trade secrets law which says, "What is yours is your experience and knowledge, what is the company's are those things which the company and its share holders have made an investment in, developed, and should be theirs to exploit." There really is no line. Those things blend and you will bear the risk of that blending.

Peter Choy

I have another scenario for Lois.

It turns out in our company we have this tiger team of people who are working on this ultra secret software, and if you know anything about software development, this is a very strange and mysterious process. It is essentially a social process but it takes place in a insular group of people. That is, commonly it takes place, in my experience at least, in development groups of very talented and insular people who relate to each other very intensively, not just a professional basis but also in terms of having very similar values and cultural lifestyles. These are very closely knit groups of people.

This particular tiger team is working on a project that nobody else in the company knows anything about. It is a secret project and the second employee of this team has just announced his resignation. Now the first member resigned a couple of weeks ago, and when the first member resigned he told me that he was just burned out and just needed to take some time off and perhaps would do some consulting and just kind of hanging out in the valley for awhile. The second employee tells me that he and the first employee are kicking around the idea of starting their own company together and kind of consulted me off-the-record about the possibility of getting some venture capitalist financing and said that there is a possibility that there were some folks he knew that they were going to approach about putting them in business.

It turns out that the venture capitalist has told these two employees that there's a real market for an advanced software product which can provide multi processing capability on Unix-based computers which happens to be exactly what this tiger team's been working on at my company.

Well as it turns out, since we work in a very security conscience company, we keep records of all the entrances and exits by employees and over the last several weeks there has been an unusual amount of midnight coming and going to this facility by the original, the two departed employees and also by two more employees who are still members of that group. I am just about to call up Lois, and it turns out that those two employees have also announced that they are leaving and when I asked them what they are going to do they won't tell me what are their future employment plans.

Now, have I been wronged? If so, what's my remedy?

Lois Abraham

This goes back to your question when you ask "Who owns something that is a trade secret?" The answer to that is kind of a strange property concept, because who owns it is whoever has developed it, given the proper care for keeping it a secret. So that means that if three companies were out there developing this particular product and each of them has built a wall of secrecy around it that's sufficient by legal standards, they each own it. But in this case, I would ask Peter "How good have you been about keeping this product secret? Have these people published papers so that they're going to be able to argue it's in the public domain? Have you had other employees in and out of that area? Do you keep track of documents? Are things locked up at night? What is the status of the precautions that you have taken?"

Peter Choy

We've built the proverbial Chinese wall around this project, hermetically-sealed.

Lois Abraham

So you feel pretty comfortable that I'm not going to walk in to court demanding a TRO and they are going to come up with the proceedings of the IEEE which detail the software.

Okay. Peter, you have a real problem. I think it's something

that could be very harmful to your company and I think that it justifies our taking action to try, at least at the front end, to get them stopped from forming another company or taking this product out to another company until we can have a preliminary injunction hearing. I think this is one where I would try to get a temporary restraining order. It would be a limited temporary order restraining their disclosure to anyone of the details or even generalities (to the extent those are secret) of their work with you, until we can get some information on what they are actually doing.

Peter Choy

And would you be seeking to take this action against all four employees or just the first two?

Lois Abraham

I think you would take action against all four employees.

Judge Ingram

What relief would you ask against the two who haven't left yet?

Lois Abraham

Well I think they are about to, they've resigned.

Judge Ingram

You can't tell them that they can't leave can you?

Lois Abraham

I suspect Peter would like to very much but I don't think we can do that. No, the relief I would ask for is a restraining order against disclosing any of the information concerning their work at SUN until we can understand more about what's going on.

Professor Howard Anawalt

Judge Ingram, I want to direct your attention to some of the things that Ron brought up in his paper. We have an employee who is leaving and occupies an important position in the company, and we have some knowledge that that employee has access to important matters and may indeed carry away some trade secrets, but in the head. And an employee having that kind of access, that kind of visi-

ble position in the company, is very nerve-racking to have leave. That can honestly be perceived on the part of Peter and the management. But on the other hand, maybe it is just a talented employee that they do not want to have competing with them who is going to set up a new company and do something that's not involving treading on any trade secrets.

Judge Ingram

And Lois is in my office asking for a TRO. Well, first of all the guy has not done anything. He is still there, he hasn't left yet. He has not done anything, he has not made any movement of any kind toward using these unidentified items of company information that you just said. I would have to know first of all, what is the imminent peril? You mean the guy is going to leave, so what! Is he going to leave and start a new company? How long is it going to take him to do that? Can he do it before we can put this on for preliminary injunction in a couple of weeks? He probably will not even be out of the place in a couple of weeks.

Professor Howard Anawalt

He's going to start up a new company, she is quite sure of that.

Judge Ingram

Okay. But is he going to do it before we can put it on calendar for a preliminary injunction on notice. And so the answer to that is that obviously he is not going to get the company started in ten days or fifteen days. So we will deny the TRO because there is no imminent threat of injury and no showing of irreparable injury because we don't even know what he's going to take with him. If he's going to take anything. What is he exposed to? All I know is he's been exposed to a lot of stuff that's unidentified, so that's out. So then we set it down for preliminary injunction and then what?

Professor Howard Anawalt

Then, who is going to have to move on the matter from that point on? Are you going to demand a good deal of persuasion from her on the identification of the trade secrets?

Judge Ingram

First of all, we have to be sure, and this is probably without

any question, but is there any adequate remedy at law of any kind? I mean does the guy have any kind of limiting agreement that's enforceable and so on. I will assume not. But don't we have to know at a minimum what the peril is, what this thing that is going to happen is that constitutes the precursor of irreparable injury?

Then we have to know exactly what it is he is going to do and we have to know that by admissible evidence through affidavits or live testimony. It has to be specifically identified. And then we have to go through the exercise of the merits of the case, you know the spectrum. Is there a probability of recovery on the part of Lois? Or at least is there a substantial triable litigating issue, and then balance the hardships. So that is what we have before us and frankly, just on what little we know so far, it does not look like it's going to fly. But maybe it will.

Lois Abraham

I think the difference between the scenario that you have just posed and the one that Peter has read is fairly broad. Yet, I would still suspect that getting a temporary restraining order on the scenario that Peter has talked about is difficult and there are going to be some factors that you will need to know.

Judge Ingram

That's in the cards. I certainly do not think there would be any problems, say, with those guys from whom you have had exit interviews and they won't talk to you, for example, and they will not tell you where they're going to go or anything. You have the one guy who goes, but he is just burnt out. That is what he says. The other guy goes, and I forgot what he said, but here you have a secret project, and the whole team goes. I mean everybody is gone. They all go sequentially. First the leader goes, and then the other guys go. So that would arouse the suspicion of the most complacent, I would think. Maybe the company is going to get hurt.

Ron Malone

Even I would say it looks like a venture capitalist is not buying an employee.

Judge Ingram

They are out there enticing.

Ron Malone

Right. He or she wants to buy the technology that Mr. Galaxy has developed and that ought to be, particularly with the toing and froing and the lack of straightforwardness, enough to raise real questions.

Peter Choy

Does it change things much if we have a witness that says these guys were not just going back and forth buying pizzas? They were taking out file boxes full of stuff at night.

Lois Abraham

That helps. That makes it an easy one. That helps. But, you do not get those very frequently.

Professor Anawalt

How do you protect American intellectual properties on the international scene?

Peter Choy

Well, you can apply for a patents abroad, for one thing. An American copyright does not go outside the continental United States. You can apply for copyrights abroad. I suspect that most of the common market countries, as an example, have some type of protection similar to ours and on the Pacific Rim I know that the Japanese have patent protection, but there are some distinct differences.

Lois Abraham

It seems to me that there may be some futility, but if you do not start at the door of the plant, you have absolutely no hope of protecting your technology on the international scene. If we cannot protect it here, we surely cannot protect it internationally.

Peter Choy

But insofar as futility is concerned, there are many CEO's in this valley who believe that insofar as the Japanese are concerned, for example, it is totally futile and all of the technology is going to Japan and it's going to be coming back here in one form or another. Furthermore, you may not be able to get a patent because the thing

that is the trade secret may have been on sale for a period of more than one year, and therefore be subject to the on-sale defense.

Lois Abraham

There are two bases for trade secrets rights. They are intangible rights. One basis of trade secret protection for the employer is the fiduciary duty of the employee during the course of employment not to do something which harms the employer. Something that would harm the employer is misappropriating or giving to someone else information or technology that the employer has developed. The fiduciary duty, depending upon the level of the employee, particularly, can end with the employment, leaving the only protection to the employer in the employment contract. Most of these contracts provide that after an employee leaves a company they will continue to observe the confidentiality and propriety of the things that they work on as the proprietary property of the employer. If there is not a contract in place, in some jurisdictions, the fiduciary duty not to harm the employer by using those trade secrets ends literally at the door.

Professor Howard Anawalt

Thank you for your attention today to the issues surrounding our tort system and its future. Thank you.

